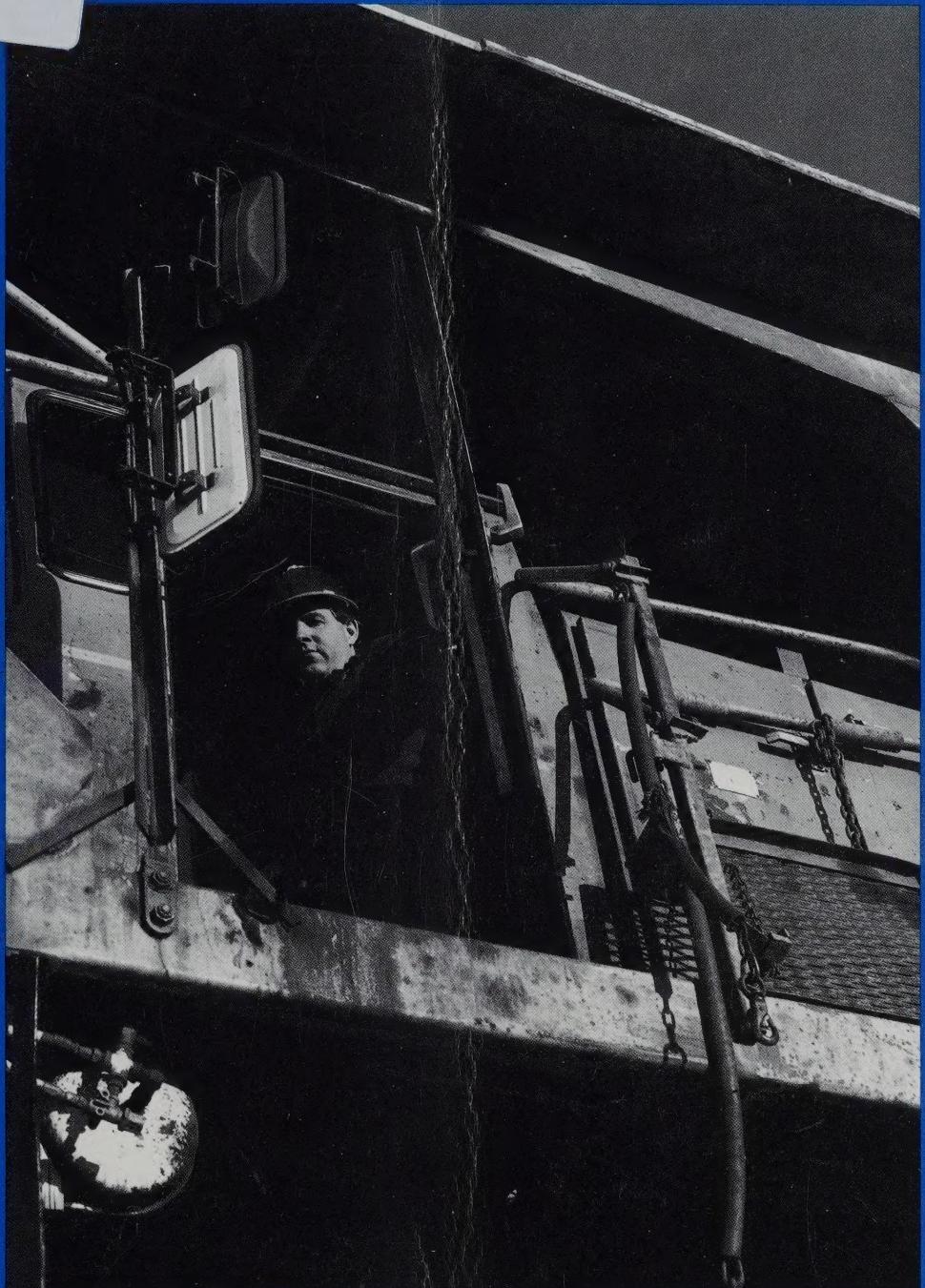


AR42



Annual Report 1985



On the cover:
Dave Webster, a
truckdriver at
Greenhills Mine,
is one of 1,900
employees who
helped Westar
Mining increase
productivity
in 1985.

Corporate Profile

Westar Mining Ltd. produces and markets coal from two surface mines in southeastern British Columbia, is a partner in the Brae oil and gas field in the United Kingdom sector of the North Sea, manages a coal port and provides consulting services.

The Company is Canada's largest exporter of metallurgical coal, used in the manufacture of steel, and a supplier of thermal coal to power plants and specialized industries.

At its Balmer Operations in Sparwood, B.C. the Company operates a truck and shovel surface mine and related coal processing facilities. Its Greenhills Operations are located near Elkford, B.C. and consist of a surface mine and processing facilities.

Marketing and customer relations activities are handled by a subsidiary, Westar Mining International Ltd. Based at the Company's Corporate headquarters in Vancouver, B.C., it has offices in Tokyo and Paris.

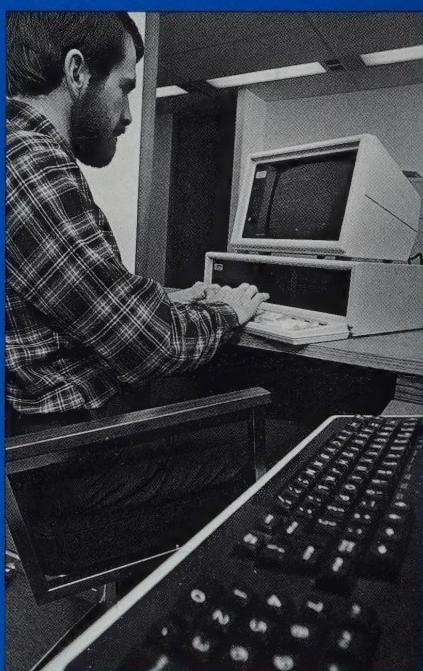
Another subsidiary, Westar Engineering Ltd. provides consulting and management services in the field of general engineering, mining, mine planning and computer systems.

Through its 7.7 percent interest in the Brae Field in the North Sea, the Company is involved in the offshore oil and gas industry. Its investment includes the South Brae oil and gas field, which came into production in 1983, the North Brae, due to come on stream in 1988 and other adjacent fields.

Westar Mining is owned 67 percent by British Columbia Resources Investment Corporation and 33 percent by Mitsubishi Corporation and nine Japanese steel mills. The Greenhills Mine is owned 80 percent by Westar Mining and 20 percent by Pohang Iron and Steel Company Limited of Korea.

The Company has about 1,900 employees and 2,000 holders of Preferred shares.

Mark Mansfield
uses computer
systems to
improve mine
efficiency.



Highlights

	1985	1984
	(Millions except number of employees)	
Operations		
Coal shipments (tonnes) — Metallurgical	6.9	7.0
— Thermal	1.2	1.1
Oil and NGL production (barrels)	2.7	2.4
Sales	\$ 614.9	\$ 621.7
Earnings before extraordinary items	34.7	40.9
Net earnings (loss)	(186.8)	26.2
Funds provided by operations	128.1	146.0
Capital expenditures	69.0	42.4
Financial Position		
Working capital	\$ 6.5	\$ 5.2
Total assets	884.6	1,181.7
Long-term debt	549.3	610.4
Shareholders' equity	(12.1)	276.8
Other Information		
Number of employees (at December 31)	1,906	2,041
Wages, salaries and employee benefits	\$ 109.2	\$ 111.1

Shipments include all coal shipped from the 80 percent owned Greenhills Mine.

Miles Oak surveys work from the cab of his mobile drill.



Review of Operations

Westar Mining achieved a solid operating performance in 1985 despite low prices and limited growth in world coal markets. Coal shipments from the Company's two surface mines in southeastern British Columbia remained stable and production from the South Brae oil and gas field surpassed the level of the previous year.

Operating gains were achieved throughout the year as further productivity improvements were implemented and cost increases were kept to a minimum. However, reduced demand from Japanese and other Pacific Rim steel producers, coupled with high coal inventories worldwide, kept constant pressure on coal prices throughout the year. As a result of these market pressures, reduced profit margins from the sale of coal led to lower earnings in 1985.

With coal prices unlikely to improve in the short term, the Company is continuing its program of streamlining operations, cutting costs and increasing productivity in all aspects of its business.

Financial results

Earnings before extraordinary items in 1985 were \$34.7 million compared to \$40.9 million the previous year.

After extraordinary items, the Company recorded a loss of \$186.8 million for the year compared to earnings of \$26.2 million in 1984. The extraordinary items in 1985 included the gain of \$72.5 million on the sale of its subsidiary, Westshore Terminals Ltd. and a \$294.0 million write-down of assets, primarily the loss on the settlement of the Bow Valley carried interest obligation. In 1984, the Company's extraordinary loss was due to the write-off of the Panel 6 hydraulic coal mine assets.

Total sales decreased by 1 percent to \$614.9 million in 1985 from \$621.7 million in 1984 as reduced coal revenues were largely offset by higher oil revenues. Coal revenues totalled \$515.1 million in 1985 compared to \$530.5 million in 1984. Revenues from the South Brae oil field totalled \$99.8 million for the year, an increase of 9 percent from the \$91.2 million recorded in 1984.

Operating profit of \$103.5 million was down from \$128.8 million in 1984. The Coal operating profit was \$71.9 million compared to \$92.6 million in 1984 and oil and gas operating profit was \$31.6 million compared to \$36.2 million the previous year.

Funds provided by operations decreased to \$128.1 million in 1985 from \$146.0 million the previous year.

Debt refinancing

The Company is involved in discussions with its lenders to obtain necessary amendments to its loan agreements. These amendments are required because of the extraordinary loss recorded in 1985 and the need to restructure these agreements. Discussions with these lenders are progressing and the Company is confident that satisfactory arrangements will be achieved.

Coal

Because of continuing tight markets for coal, the Company has taken a number of steps to reduce its costs and increase productivity. These included reducing manning levels at Balmer Mine, continuing all cost reduction programs, and closing underground operations. The Company has attempted to minimize the affect of soft coal markets on its employees by using shutdowns wherever possible to reduce inventories.

An aggressive marketing campaign in the Far East, Europe and South America resulted in new sales for Balmer and Greenhills coal.

Sales to new customers in Europe accounted for more than 1 million tonnes in both 1984 and 1985.

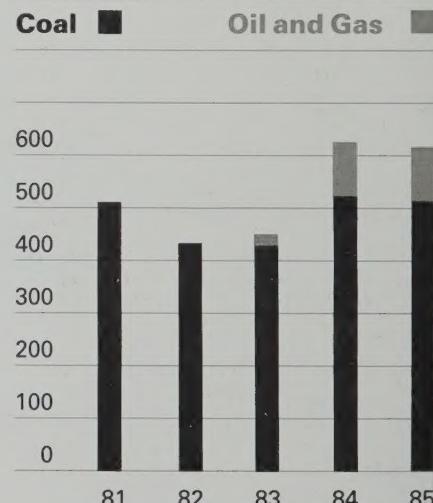
Total shipments from the two mines totalled 8.1 million tonnes, the same level as in 1984. Shipments from Balmer Mine amounted to 5.2 million tonnes of metallurgical coal and 0.6 million tonnes of thermal coal. These shipments are up slightly from the 5.2 million tonnes of metallurgical and 0.3 million tonnes of thermal coal shipped in 1984.

Greenhills Mine, 80 percent owned by Westar Mining, shipped 1.7 million tonnes of metallurgical coal and 0.6 million tonnes of thermal coal in 1985. This compares to 1.8 million tonnes of metallurgical coal and 0.8 million tonnes of thermal coal shipped in 1984.

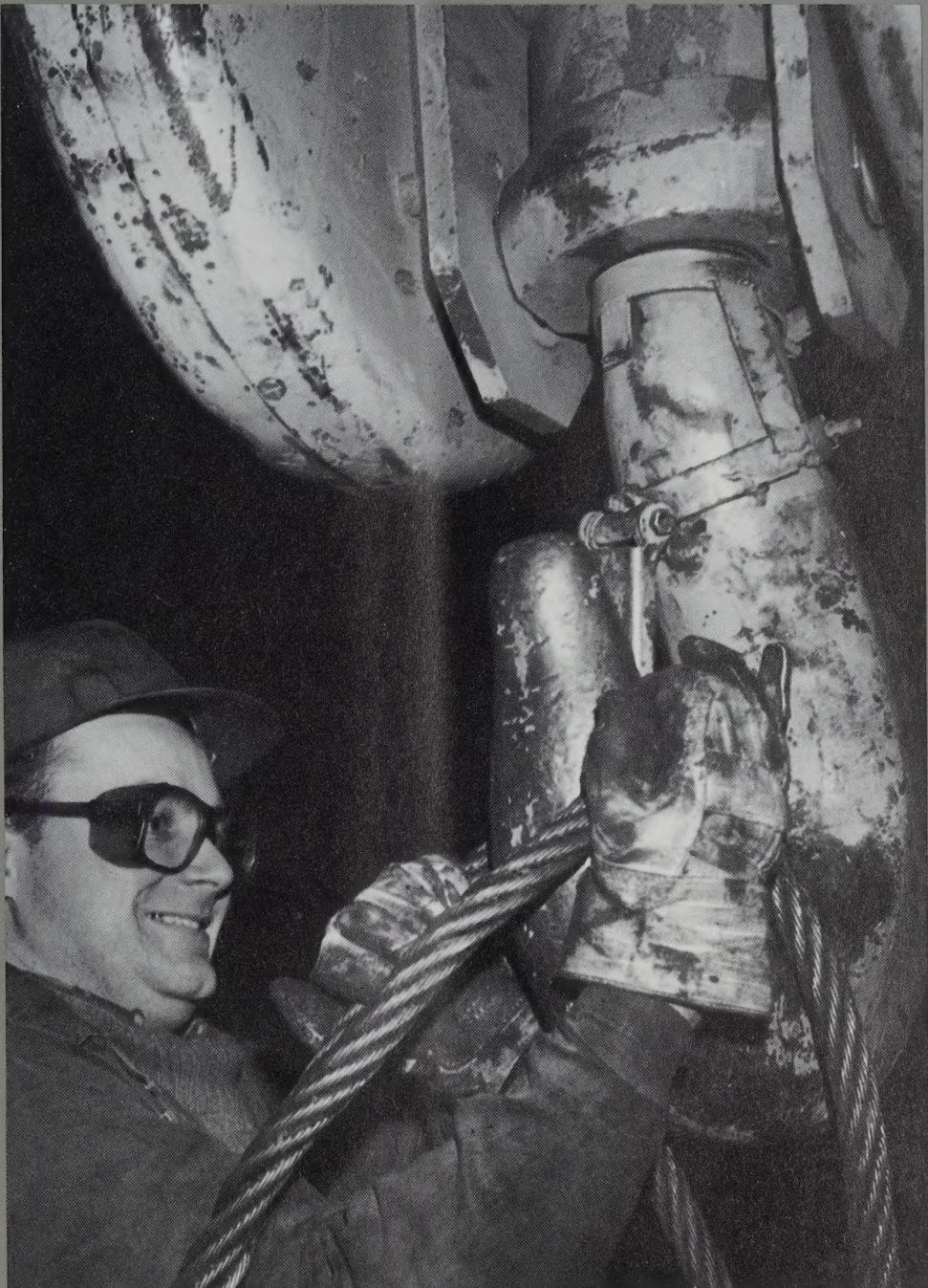
Balmer Operations were shut down for 1½ weeks in 1985 to reduce inventories. A 15 day shutdown beginning March 1986 will reduce Balmer inventories by about 200,000 tonnes and a further shutdown is tentatively scheduled for August.

Sales

(Millions of Dollars)

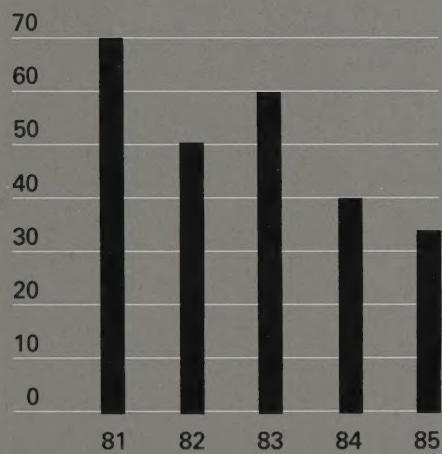


**Wray Mills hooks
a heavy cable
sling to a boom
during repairs.**



**Earnings Before
Extraordinary Items**

(Millions of Dollars)



Greenhills Operations underwent six weeks of shutdowns in 1985 due to slower than expected sales and some delays in shipping the product to the customer. The Greenhills Mine was closed for two weeks in February 1986 and will be shut down for an additional two weeks beginning March 1986.

In late 1985, the Company announced plans to further reduce costs by advancing the previously announced closure of its remaining underground mine, combining some departments and continuing staff wage freezes. These cuts reduced manning levels by about 190 employees and will help the Company maintain its competitive position in the years ahead. A job placement program found employment for a majority of displaced employees.

Oil and Gas

Westar Mining's investment in the South Brae field in the North Sea marked its second full year of operations in 1985 with record production and a good operating performance.

The Company's 7.7 percent share of production amounted to 2.7 million barrels of oil and natural gas liquids, an increase of 11 percent from 1984 levels. Total production from the field was 35 million barrels for the consortium of eight companies which financed its development. Oil prices remained firm throughout 1985 but began to fall dramatically at year end.

The Company reached agreement with Bow Valley Industries to cancel Westar Mining's obligation to continue financing Bow Valley's 7.7 percent of development costs. Bow Valley paid \$20.9 million to be relieved of Westar Mining's loans of U.S. \$203 million. This agreement cancels Westar Mining's commitment to continue financing Bow Valley's considerable

obligations and significantly reduces the Company's exposure to changes in world oil prices.

Development of the adjacent North Brae field remained on schedule and below budget in 1985. Major contracts for the construction of the support jacket and production components have been let. The Company's share of capital expenditures on the North Brae project totalled about \$45 million in 1985, with an equal amount invested on behalf of Bow Valley.

Westshore Terminals

In April 1985, the Company sold its 100 percent interest in Westshore Terminals Ltd. to B.C. Resources Investment Corporation for \$115 million. As part of the sale, Westshore repaid an existing loan from Westar Mining of \$90 million.

Marketing

In January 1986, the Company's marketing organization, Westar Mining International Ltd. concluded negotiations with Japanese steel mills for metallurgical coal from Balmer Mine for the year beginning April 1, 1986. Under the terms of this new agreement, the Japanese will pay U.S.\$49 per tonne for Balmer metallurgical coal which at prevailing exchange rates was approximately 40 cents below the previous year's price of CDN \$69.09. The price reduction follows a one-year price freeze for the coal year beginning April 1, 1985.

During negotiations, the Japanese also said they would take 50 percent of their contracted volume of 4.3 million tonnes from the Company.

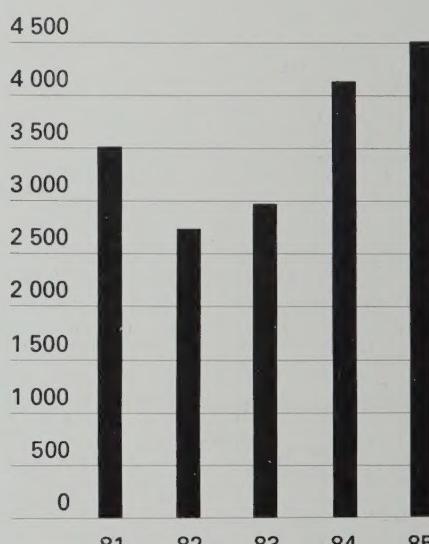
In separate negotiations, the Japanese steel mills agreed to a one-year extension of the Greenhills coal contract. Beginning April 1, 1986 they will pay U.S. \$49.50 per tonne compared to CDN \$81.50 per tonne in 1985. The Japanese stated they would purchase about 50 percent of the base contract volume of 760,000 tonnes.

The Company also signed an agreement with Pohang Iron and Steel Company (POSCO) of South Korea to extend the purchase of coking coal from Balmer Mine for an additional five years. The agreement calls for Westar Mining to supply 4.6 million tonnes to POSCO through to the end of the contract on March 31, 1990. POSCO is also a major customer for Greenhills coal and owns 20 percent of the mine.

The marketing group continues to pursue new opportunities for growth throughout the Pacific Rim and Europe. The development of a market for semi-coking coal produced at Balmer Mine provides an opportunity for continued growth for this new product.

Employee Productivity

(Tonnes of Clean Coal per Employee)



Four Japanese steel mills purchased 430,000 tonnes of semi-coking coal from Balmer during 1985 and have contracted to purchase 650,000 to 850,000 tonnes in 1986.

Engineering

Westar Engineering Ltd., the Company's consulting subsidiary, continued the steady progress begun the previous year. Considerable work was devoted to seeking out new contracts for mine management consulting, computer systems and mine technology.

The Company is actively pursuing a number of promising activities in India, one of which has received financial support from the Canadian International Development Agency.

Labor

Negotiations are continuing for new collective agreements at the Greenhills and Balmer mines. The Balmer contract with the United Mine Workers of America, which represents about 1,000 employees, expired on December 31, 1985.

Gary Lobban performs detailed analysis of a coal sample.



Negotiations with the Greenhills Workers' Association, which represents approximately 400 employees, have been ongoing for approximately one year.

Outlook

The continuing oversupply of coal and crude oil on world markets offers little hope of price improvement in these markets in the short term. Prices will continue under constant downward pressure throughout 1986, with an unsettled international oil market and price.

The price of crude oil from the Company's North Sea operations remained stable throughout 1985, but began to drop precipitously at year end. In March 1986, North Sea crude was selling for about U.S.\$12 compared to U.S.\$30 in December 1985.

Metallurgical and thermal coal prices will continue to come under downward pressure because of oversupply in the marketplace.

Interest rates will impact on Company earnings in 1986 because of the Company's \$466 million of floating rate long-term debt. Almost all of the Company's revenues are in U.S. dollars, so the Company should benefit from any decline in the value of Canadian currency.

Canadian coal suppliers will continue to face tough competition from producers in other nations, particularly South Africa and Australia. Their lower costs, closer access to markets and devalued currencies provide substantial advantages.

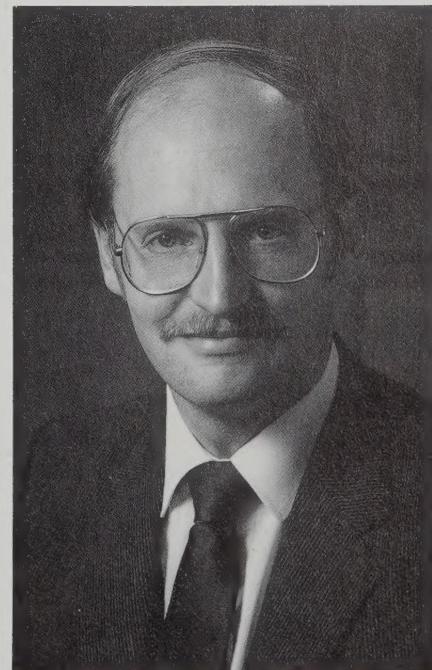
The Company firmly believes that its coal operations will remain competitive with other world suppliers through productivity improvements and stringent cost controls. However, the substantial drop in world oil prices will depress Company earnings in 1986. The challenge for Westar Mining in the year ahead will be to seek new ways of reducing costs, remaining competitive and ensuring the long term financial stability of shareholders' investment.

On behalf of the Board of Directors,

Bruce I. Howe
Chairman

Gary K. Livingstone
President

March 27, 1986



Gary K. Livingstone
President

Financial Summary

Highlights

Intense competition in the marketplace continued to squeeze coal profit margins in 1985. Sales volumes and prices were maintained through an aggressive marketing strategy while cost increases were kept to a minimum through productivity improvements and staff reductions.

Oil and gas revenues from the South Brae field increased in 1985 due to higher production levels.

Effective April 1, 1985 the Company sold its subsidiary, Westshore Terminals to Westar Industries, a subsidiary of B.C. Resources. Consequently, the 1985 financial results include Westshore for the first quarter only. In conjunction with this sale Westshore repaid \$90 million in advances to the Company which in turn paid a \$95 million dividend to its common shareholders. Westar Industries loaned \$63 million, its share of the dividend, back to the Company.

Because of continuing low commodity prices due to the world oversupply situation, the Company undertook a major review of all assets during the fourth quarter of 1985, to assess whether the carrying value would be recovered through use or by sale. As a result of the review, and the agreement reached with Bow Valley Industries of Calgary to cancel a Brae Field funding obligation, the carrying value of certain assets was written down on the books of the Company and recorded as an extraordinary item.

Financial data relating to the Company's two major business segments can be found in Note 16 to the consolidated financial statements. Reference to this material will assist the reader in reviewing the Company's operating results.

Earnings

Consolidated earnings before extraordinary items in 1985 were \$34.7 million compared to \$40.9 million in 1984. An extraordinary charge to earnings of \$221.5 million resulted in a net loss of \$186.8 million in 1985. Net earnings in 1984 were \$26.2 million after recording an extraordinary loss of \$14.7 million. These extraordinary items are described in Note 12 to the financial statements.

Operating profit from coal operations for 1985 was \$71.9 million compared to \$92.6 million in 1984. Operating profit generated from the South Brae field amounted to \$31.6 million in 1985 compared to \$36.2 million in 1984.

Coal

Combined revenues from operations declined slightly in 1985 due primarily to the sale of Westshore Terminals at the end of the first quarter. Revenues from sales of coal products increased slightly in 1985 as an increase in volume at Balmer was partially offset by a reduction in volume at Greenhills. Prices stayed relatively constant over the two years, despite the replacement of some traditional products with lower priced coals, due primarily to an improved exchange rate for U.S. dollar denominated sales.

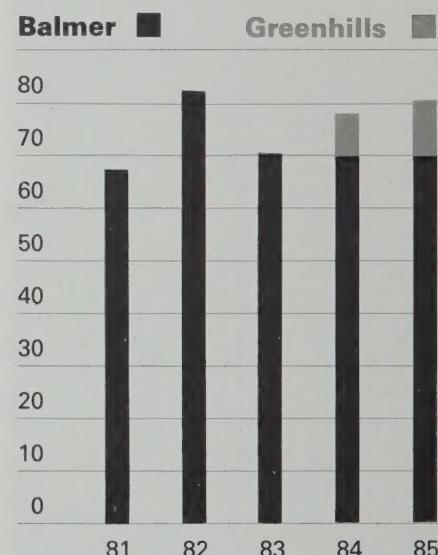
The contract price for the sale of Balmer metallurgical coal to the Japanese Steel Mills, which is also the basis of pricing for other Pacific Rim customers, remained unchanged on April 1, 1985 at \$69.09 per tonne. The contract price for Greenhills metallurgical coal to its Pacific Rim customers continued to escalate in 1985 as per the contracts. For the 1986 coal year, metallurgical coal sold to the Japanese Steel Mills under contract is priced at U.S. \$49 for Balmer and U.S. \$49.50 for Greenhills.

Thermal coal prices improved slightly in 1985 due primarily to the stronger U.S. dollar.

Operating costs increased by 5 percent in 1985 despite rigorous cost controls and staff reductions due primarily to the increase in the ratio of overburden removed to clean coal produced at both mines. The impact of the staff reductions which occurred in the fourth quarter of 1985 will not be felt until 1986.

Depreciation, depletion and amortization expense decreased to \$31.0 million in 1985 from \$45.3 million in 1984. The principal reasons for the decrease were the closure of the underground hydraulic mine at the end of 1984, the sale of Westshore Terminals at the end of the first quarter 1985 and mine shutdowns during the year.

Metallurgical Coal Prices (April 1) (Dollars per Tonne)



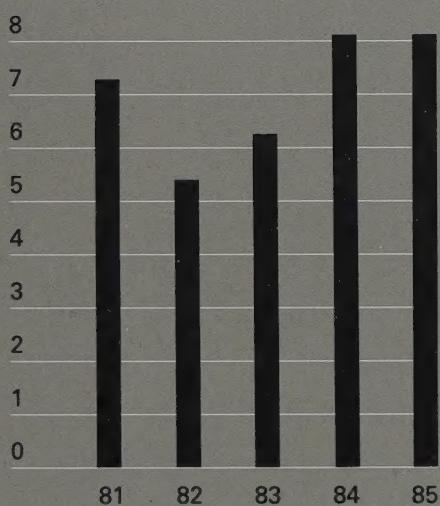
Effective April 1, 1986 Balmer coal will be sold at U.S. \$49 and Greenhills coal at U.S. \$49.50.



**Brian Machan
and Art Saran test
a bulldozer's
electric system.**

Total Coal Shipments

(Millions of Tonnes)



Includes all coal shipped from the 80 percent owned Greenhills Mine.

Oil and Gas

The oil and gas segment represents the Company's 7.7 percent investment in the Brae Field which is located in the U.K. sector of the North Sea. Revenues increased by 9 percent in 1985 due to an increase in production volumes. The average price per barrel was approximately CDN \$38.00 for both years as the effects of the reduction in the U.S. dollar price per barrel were largely offset by the weakening of the Canadian dollar. Total costs and expenses increased by 24 percent during 1985 due primarily to higher provisions for depletion and petroleum revenue tax.

The dramatic fall in world oil prices in recent months will have a substantial impact on the Company's financial results in 1986.

Interest

Total interest cost on long-term borrowings decreased by \$17.7 million to \$61.9 million in 1985 due to lower interest rates and lower debt balances. Interest expense, net of interest income received on the Bow Valley advances and capitalized interest, amounted to \$35.8 million in 1985 compared to \$47.9 million in 1984.

Funds Provided by Operating Activities

Funds generated by operating activities amounted to \$110.0 million in 1985 compared to \$157.9 million in 1984. The decrease is due primarily to a lower level of earnings and an increase in inventory levels. In 1984, funds provided by operating activities included a decrease in inventories of \$16.6 million.

Capital Expenditures

Capital expenditures increased to \$69.0 million in 1985 from \$42.4 million in 1984. The increase in spending was all related to the development of the North Brae field. The field is due to commence production in late 1988. Capital expenditures for coal and port

operations remained relatively flat at \$13.3 million for 1985. The majority of these expenditures related to equipment additions at the Greenhills Mine and pollution control spending at the Balmer Mine.

Long-Term Debt

Long-term debt decreased to \$549.3 million at December 31, 1985 from \$610.4 million at the end of 1984. The decrease was primarily due to the loan from Westar Industries as the majority of funds from operations were applied to capital expenditures and advances to Bow Valley under our carried interest obligation in the Brae Field. The Canadian dollar equivalent of U.S. dollar denominated debt outstanding at year-end compared to December 31, 1984 was affected by the weaker Canadian dollar. The exchange rate for the U.S. dollar in terms of the Canadian dollar at December 31, 1985 was 1.3975 compared to 1.3214 a year earlier. This had the effect of increasing long-term debt at December 31, 1985 by \$27.9 million.

However, the Company's U.S. dollar denominated product sales act as a natural hedge against exchange fluctuations in its U.S. dollar debt.

Refinancing Discussions

The extraordinary write-downs at December 31, 1985 eliminated the book equity of the Company. As a result, the Company is carrying out discussions with its lenders to obtain amendments to its debt equity covenants and to restructure these agreements. The Company is confident that these discussions will be satisfactorily concluded as the lenders have expressed their desire to negotiate amended agreements.

Management's Responsibility for Financial Reporting

The information and consolidated financial statements in the Annual Report are the responsibility of management and the Board of Directors of the Company. The consolidated financial statements have been prepared by management in accordance with generally accepted accounting principles.

Touche Ross & Co., who were appointed by the Common shareholders as the Company's auditors, have examined the consolidated financial statements in order to express their opinion as to whether the statements present fairly the Company's financial position, results of operations and changes in financial position, in accordance with generally accepted accounting principles applied on a consistent basis. This report is presented with the consolidated financial statements.

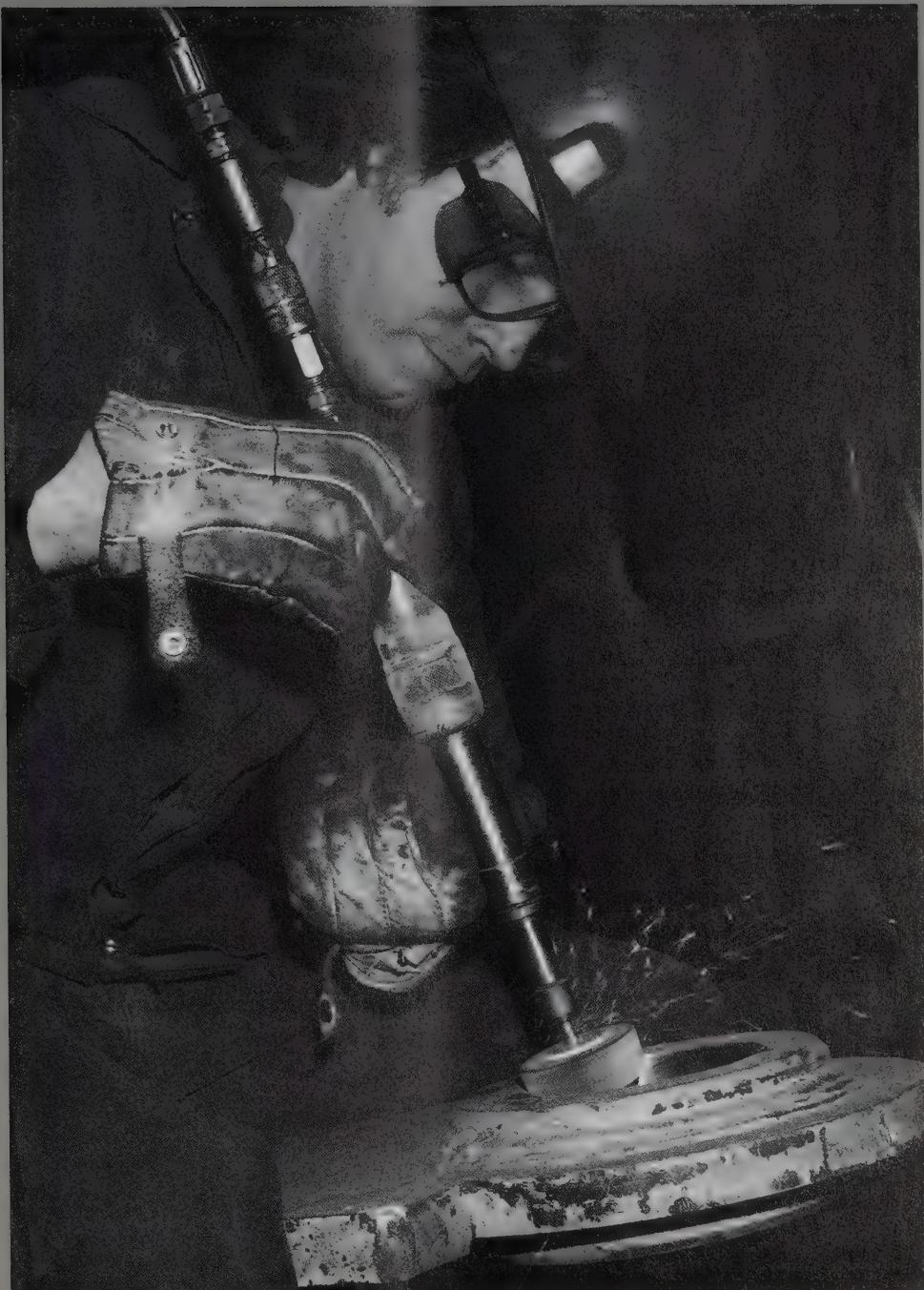
The Audit Committee of the Board of Directors meets with management and the auditors to ensure that they are fulfilling their responsibilities and reviews with them the consolidated financial statements before approval of the statements by the Board of Directors.

Stan Hildebrandt
works on a wheel
motor at Balmer
Mine.



Chuck Gibson
makes a needed
repair at Balmer's
maintenance
centre.

9



Dagney Vermunt
helps marketing
arm sell coal
around the world.

Westar Mining Ltd.

**Consolidated
Statement of
Earnings**

For the year ended
December 31, 1985

Note
Reference

1985

(Millions)

1984

Sales	15,16	\$ 614.9	\$ 621.7
Costs and expenses			
Cost of products sold		433.1	408.7
General and administrative		11.4	10.9
Depreciation, depletion and amortization		66.9	73.3
		511.4	492.9
Operating profit		103.5	128.8
Financing costs	9	35.8	47.9
Other (income) expenses	10	(3.6)	.2
		32.2	48.1
Earnings before income taxes and extraordinary items		71.3	80.7
Provision for income taxes	11	36.6	39.8
Earnings before extraordinary items		34.7	40.9
Extraordinary items	12	(221.5)	(14.7)
Net earnings (loss)		(186.8)	26.2
Less: Dividends on Preferred shares		4.6	4.6
Net earnings (loss) attributable to Common shareholders		\$(191.4)	\$ 21.6
Earnings (loss) per Common share			
Before extraordinary items		\$ 1.65	\$ 1.99
Net earnings (loss)		(10.49)	1.18

Westar Mining Ltd.
Consolidated
Balance Sheet
As at December 31, 1985

Assets	Note Reference	1985 (Millions)	1984
Current			
Accounts receivable	3	\$ 35.7	\$ 33.2
Inventories	3	56.4	50.0
		92.1	83.2
Property, plant, equipment and related development costs, net	16	633.8	826.5
Exploration and development advances	4,12	20.9	243.5
Investment in related company	5	115.0	—
Other assets		22.8	28.5
		\$ 884.6	\$1,181.7
11			
Liabilities and Shareholders' Equity			
Current			
Bank indebtedness		\$ —	\$ 5.6
Accounts payable and accrued liabilities		74.0	65.8
Income taxes payable		—	6.6
Current portion of long-term debt	2,6	11.6	—
		85.6	78.0
Long-term debt	2,6	549.3	610.4
Due to related company	5	66.9	—
Deferred income taxes		194.9	216.6
Shareholders' equity			
Share capital	7	63.2	63.2
Contributed surplus		15.2	15.2
Retained earnings (deficit)		(95.5)	190.9
Translation adjustments		5.0	7.4
		(12.1)	276.7
Commitments and contingencies	8		
		\$ 884.6	\$1,181.7

Approved by the Directors:

Director

Director

Westar Mining Ltd.
Consolidated
Statement of
Changes in
Financial Position

For the year ended
 December 31, 1985

Note Reference	1985 (Millions)	1984
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Operating Activities

Funds provided by operations	13	\$ 128.1	\$ 146.0
Reduction (increase) in working capital		(13.5)	16.5
Dividends on Preferred shares		(4.6)	(4.6)

Funds provided

Funds provided	110.0	157.9
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Investing Activities

Additions to property, plant and equipment		(69.0)	(42.4)
Exploration and development advances:			
Amounts advanced		(74.9)	(55.0)
Repayments received		49.5	51.9
Sale of subsidiary	12,15	88.9	—
Other		3.8	.3

Funds provided (invested)

Funds provided (invested)	(1.7)	(45.2)
----------------------------------	--------------	--------

Financing Activities

Repayments of long-term debt		(74.6)	(118.0)
Advances from Westar Industries Ltd.		66.9	—

Funds provided (applied)

Funds provided (applied)	(7.7)	(118.0)
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Dividends on Common shares

Dividends on Common shares	(95.0)	—
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Increase (decrease) in cash

Bank indebtedness at beginning of year		5.6	(5.3)
		(5.6)	(.3)

Bank indebtedness at end of year

Bank indebtedness at end of year	\$ —	\$ (5.6)
----------------------------------	------	----------

Westar Mining Ltd.
Consolidated
Statement of
Retained Earnings

For the year ended
 December 31, 1985

	1985	1984
	(Millions)	
Retained earnings at beginning of year	\$ 190.9	\$ 169.3
Net earnings (loss)	(186.8)	26.2
Dividends — Preferred shares	(4.6)	(4.6)
— Common shares	(95.0)	—
Retained earnings (deficit) at end of year	\$ (95.5)	\$ 190.9

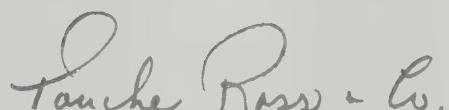
Auditors' Report

To the Shareholders of
 Westar Mining Ltd.

13

We have examined the consolidated balance sheet of Westar Mining Ltd. as at December 31, 1985 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Company as at December 31, 1985 and the results of its operations and the changes in its financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.



Touche Ross & Co.
 Chartered Accountants

Vancouver, British Columbia
 January 29, 1986

Westar Mining Ltd.
Notes to the Consolidated
Financial Statements

December 31, 1985

14

1. Summary of Significant Accounting Policies

Accounting Principles:

The Company is incorporated under the Company Act of the Province of British Columbia and prepares its accounts in accordance with generally accepted accounting principles followed in Canada.

Principles of Consolidation:

The consolidated financial statements include the accounts of all subsidiaries. The principal subsidiary is Westar Holdings (U.K.) Limited. The Company has an 80% interest in the Greenhills Mine Joint Venture which is proportionately consolidated.

Translation of Foreign Currencies:

Assets and liabilities denominated in foreign currencies are translated at rates of exchange in effect at the balance sheet date; revenue and expenses are translated at rates prevailing during the year. Provisions for exchange gains and losses arising on translation of foreign currency denominated items and gains and losses realized on transactions completed during the year are included in earnings. Exchange fluctuations relating to the translation of the investment in the United Kingdom oil and gas operations are deferred as a separate component of shareholders' equity.

Inventories:

Coal inventories are valued at the lower of average cost and net realizable value. Depreciation, depletion and amortization are not included in coal inventory costs. Operating supplies are valued at average cost less a provision for obsolescence.

Property, Plant, Equipment and Related Development Costs:

Property, plant and equipment are stated at cost. During the construction or development stages of major capital projects, interest is capitalized as a cost of these projects on the basis of expenditures incurred without restriction to specific borrowings for these projects. Replacements and major improvements are capitalized. Costs of assets sold, retired or abandoned and the related amounts of accumulated depreciation are eliminated from the accounts. Gains or losses on such dispositions are included in earnings. Expenditures for repairs and maintenance of plant and equipment are charged against earnings. Plant and equipment is depreciated on a unit of production method over the estimated useful lives of the assets.

Acquisition costs of coal reserves are capitalized and depleted by the unit of production method. Coal exploration costs are charged against earnings when incurred. Costs incurred in connection with feasibility studies for new mining projects are capitalized and charged against earnings over the life of the mine or written off when it is determined that the project is not feasible. Preproduction and development costs are capitalized and amortized on the straight line basis over the life of each mine.

Oil and gas properties are accounted for using a form of the full cost method whereby all acquisition, exploration and development costs are capitalized as incurred by cost centre and are depleted on the unit of production method. The Company carries its oil and gas properties at the lower of capitalized cost or net recoverable

value. The recoverability of costs capitalized net of accumulated depletion is reviewed annually based on estimates of proven oil and gas reserves, prices and costs in effect at the balance sheet date. Costs related to certain unproven oil and gas properties are excluded from costs subject to depletion. These properties are reviewed periodically to assess the extent to which the carrying value has been impaired with any required provision for impairment being included in costs subject to depletion and to the annual assessment of carrying values.

Pension Plans:

Annual contributions to employee pension plans are charged against earnings. Pension contributions are actuarially determined to include amounts necessary to provide for current service and for funding of past service liabilities over 15 years.

Income Taxes:

Income taxes are accounted for by the tax allocation method, whereby the provision for taxes is made in the year transactions affect net earnings rather than when such items are recognized for tax purposes. Differences between the provision for taxes and taxes currently payable are reflected as deferred income taxes. Tax benefits from earned depletion are reflected as a reduction in the provision for income taxes. Investment tax credits claimed are deducted from the related capital expenditures.

2. Refinancing Discussions

The Company is carrying out discussions with its lenders to obtain amendments to its bank credit agreements. The amendments are necessary as a result of the extraordinary write-downs in 1985 and the need to restructure these agreements.

The Company is confident that these discussions will be satisfactorily concluded as the lenders have expressed their willingness to negotiate amended agreements.

These consolidated financial statements have been prepared on the assumption that the Company will be successful in obtaining the amended agreements. Continued operations are dependent upon the resolution of these matters. The carrying value of assets and classification of long-term debt could be significantly different if these matters are not resolved.

3. Inventories

	1985	1984
	(Millions)	
Coal	\$38.1	\$27.9
Operating Supplies	18.3	22.1
	\$56.4	\$50.0

4. Exploration and Development Advances

These advances were made pursuant to the Company's carried interest obligation to finance for another participant an amount equivalent to its share of exploration and development costs relating to its interests in several licenses for exploration and development of the Brae oil and gas field in the United Kingdom sector of the North Sea (see Note 8).

Agreement has been reached with the participant to settle its liability under the carried interest obligation and to terminate the agreement. The proceeds on settlement of \$20.9 million will be utilized to pay down borrowings under the credit facility (see Note 6). The loss on the transaction has been recorded as an extraordinary item (see Note 12). The United Kingdom subsidiaries are contingently liable up to U.S. \$10 million for tax adjustments, relating to the participant, that may arise as a result of the transaction.

5. Sale of Subsidiary to Related Company

Effective April 1, 1985, the Company sold its wholly owned subsidiary Westshore Terminals Ltd. to Westar Industries Ltd., a wholly-owned subsidiary of British Columbia Resources Investment Corporation, for 115,000 cumulative redeemable Class C Preferred shares of Westar Industries of \$1,000 par value each. B.C. Resources through a wholly owned subsidiary owns 66.6% of the outstanding Common shares of the Company.

The shares pay quarterly dividends based on 70% of the prevailing prime rate of a Canadian chartered bank and carry a mandatory redemption provision whereby Westar Industries will redeem one third of the shares outstanding on each of March 31, 1990, March 31, 1991 and March 31, 1992.

In conjunction with the sale of Westshore, the Company paid a \$95 million dividend to its Common shareholders. Westar Industries in turn loaned \$63.2 million, its share of the dividend, to the Company. Interest on the loan, which is calculated based on the prevailing prime rate of a Canadian chartered bank plus one percent, is added to the principal outstanding until such time as the principal amount reaches the amount of the Westar Industries Preferred shares outstanding. The loan is repayable on demand providing that the loan amount outstanding after such payment is equal to or greater than the amount of the Westar Industries preferred shares outstanding.

6. Long-term Debt

	1985	1984
	(Millions)	
Bank Credit Agreements		
\$70 million credit facility	\$ 70.0	\$ —
\$300 million credit facility	—	298.7
U.S. \$300 million credit facility		
Westar Mining Ltd.	59.2	—
Westar Holdings (U.K.) Ltd.	320.9	—
South Brae Field Credit Agreement	108.3	287.4
Other	2.5	24.3
	560.9	610.4
Less: Current portion	11.6	—
	\$549.3	\$610.4

Bank Credit Agreements:

Borrowings under these agreements can be in bankers' acceptances or direct borrowings in Canadian dollars, U.S. dollars or Eurocurrencies with interest based on Canadian prime rate, U.S. base rate or London Interbank Offered Rate (LIBOR) respectively. The interest rate on U.S. \$60 million has been fixed at 12.5% through an interest rate swap agreement expiring October, 1990. The average cost of borrowings under these agreements at December 31, 1985 was 9.8%.

The amount borrowed under the U.S. \$300 million credit facility, which at December 31, 1985 was U.S. \$272 million is a revolving loan which converts to a term loan on June 29, 1991. The facility can be accessed in either the United Kingdom or Canada. The principal outstanding at the conversion date is to be repaid through twelve equal semi-annual installments commencing June 30, 1991. The lender under this facility has the option of reducing the facility by U.S. \$50 million on each of June 30 and December 31, 1986. The option to reduce the facility at June 30 has been exercised. The advance outstanding has been classified as long-term debt since discussions are taking place to defer for at least one year the lender's option of reducing the facility.

The principal outstanding under the \$70 million credit facility is to be repaid in fourteen equal semi-annual installments commencing January 2, 1986.

South Brae Field Credit Facility:

The outstanding balance of this syndicated credit facility is secured by charges on the interests of the Company's United Kingdom subsidiaries in the licences, assets and revenues relating to the South Brae field and is guaranteed by Westar Mining. The loan bears interest based on LIBOR and at December 31, 1985 the average interest cost was 9%. The balance of U.S. \$77.5 million is repayable by payments of U.S. \$23 million by January 31, 1986, U.S. \$15.5 million by June 30, 1986 and U.S. \$39 million by January 2, 1987 from proceeds from settlement of the carried interest obligation (see Note 4), future production proceeds or unutilized existing long-term credit facilities. Accordingly, the 1986 installment has been classified as long-term debt.

7. Share Capital

	1985	1984
	(Millions)	
Authorized		
5,000,000 Class A Preferred shares of \$25 par value each		
28,000,000 Common shares of \$1 par value each		
Issued		
1,799,500 \$2.5625 Cumulative Redeemable Class A Preferred shares, Series 1	\$45.0	\$45.0
18,247,530 Common shares	18.2	18.2
	\$63.2	\$63.2

The Preferred shares may be issued from time to time in one or more series having special rights and restrictions fixed prior to issue of each series by the directors of the Company.

The Series 1 Preferred shares are retractable at the option of the holder on April 15, 1989 and October 15, 1992 at \$25 per share plus accrued and unpaid dividends. The shares are redeemable commencing April 15, 1989 at \$26.25, declining annually to \$25 on April 15, 1993.

Effective July 1, 1985, the Company became obliged to make all reasonable efforts to purchase quarterly, at prices not exceeding \$25, a specified quantity of shares not exceeding one percent of the outstanding shares. The Company purchased and cancelled 500 shares in 1985.

8. Commitments and Contingencies

The Company, through its United Kingdom subsidiaries, has interests in several licences for the exploration and development of the Brae oil and gas field in the United Kingdom sector of the North Sea. Production commenced in 1983 in an area designated as the South Brae field in which the Company holds a 7.7% working interest. Development has commenced in an area designated as the North Brae field. The Company estimates its 7.7% share of future capital expenditures relating to North Brae will be \$125 million until production commences late in 1988.

The Company has guaranteed the lease commitment of a related company requiring minimum annual rental payments of \$7.0 million in 1986, \$7.0 million in 1987, \$8.8 million in 1988, \$9.1 million in 1989 and \$9.1 million in 1990. Minimum annual rental payments will escalate to \$26.1 million by 2002.

9. Financing Costs

	1985	1984
	(Millions)	
Interest expense		
Long-term debt	\$ 61.9	\$ 79.6
Other	2.9	—
Less: interest charged to major capital projects	(4.7)	(6.7)
	60.1	72.9

Interest income

Exploration and development advances	(24.3)	(25.0)
	\$ 35.8	\$ 47.9

10. Other (Income) Expenses

	1985	1984
	(Millions)	
Dividends from related company	\$ (5.8)	\$ —
Other	2.2	.2
	\$ (3.6)	\$.2

11. Provision for Income Taxes

	1985 (Millions)	1984
Current		
Federal and provincial income taxes	\$ 8.7	\$ 5.3
British Columbia mining tax	1.4	2.7
	10.1	8.0
Deferred		
Federal and provincial income taxes	5.7	13.0
British Columbia mining tax	1.5	3.5
United Kingdom corporation tax	19.3	15.3
	26.5	31.8
	\$ 36.6	\$ 39.8

The difference between the income tax rates recorded and those obtained by applying the combined federal and provincial statutory rates is as follows:

	1985	1984
Statutory federal and provincial income tax rate	52.0%	52.0%
Increase (decrease) resulting from:		
Non-deductible payments to provincial governments for mining taxes, royalties and mineral land tax	8.7%	10.0%
Federal resource allowance	(9.7%)	(9.7%)
Earned depletion	(2.0%)	(3.6%)
Other	2.3%	0.6%
Effective tax rate	51.3%	49.3%

The Company has accumulated earned depletion benefits available to reduce the provision for income taxes in future years by approximately \$10.6 million.

12. Extraordinary Items

	1985 (Millions)	1984
Loss on settlement of carried interest obligation net of income taxes of \$9.6 million	\$(279.4)	\$ —
Adjustments to carrying value of assets net of income taxes of \$13.6 million	(14.6)	—
Sale of Westshore Terminals Ltd. net of income taxes of \$9.0 million	72.5	—
Loss on closure of the underground hydraulic mine, net of income taxes of \$18.6 million	—	(14.7)
	\$(221.5)	\$(14.7)

During the fourth quarter of 1985, the Company undertook a review of its assets in order to assess whether the carrying value would be recovered through use or by sale. As a result of the review, it was determined that adjustments of carrying values aggregating \$14.6 million after income taxes were required.

13. Funds Provided by Operations

	1985 (Millions)	1984
Earnings before extraordinary items	\$ 34.7	\$ 40.9
Add: Items not affecting working capital		
Depreciation, depletion and amortization	66.9	73.3
Deferred income taxes	26.5	31.8
	\$128.1	\$146.0

14. Pension Plans

The Company has pension plans for hourly and salaried employees which at December 31, 1985 had no unfunded past service liabilities.

15. Related Party Transactions

The Company sells metallurgical coal produced from its Balmer mines to Mitsubishi Corporation for resale to nine Japanese corporations under an agreement expiring on March 31, 1990. The Company sells metallurgical coal produced from its Greenhills Mine directly to the nine Japanese corporations under contracts which expire on March 31, 1986. The buyers have signed a letter of intent to extend these contracts beyond the current expiry date. At December 31, 1985, Mitsubishi Corporation together with the nine Japanese corporations owned 33.4% of the Company's outstanding Common shares. Sales to these Japanese customers amounted to \$263 million and \$254 million for the years ended December 31, 1985 and 1984 respectively.

Pohang Iron and Steel Company Limited of Korea, which has a 20% interest in the Greenhills Mine Joint Venture, purchases Balmer and Greenhills metallurgical coals from the Company under long-term contracts extending through March 31, 1990 and 2002 respectively. Sales to Pohang amounted to \$65 million and \$72 million for the years ended December 31, 1985 and 1984 respectively.

Effective April 1, 1985, the Company sold Westshore Terminals Ltd. to Westar Industries Ltd. for \$115 million in Westar Industries Ltd. Preferred shares. The resultant gain of \$72.5 million has been recorded as an extraordinary item.

The Company ships substantially all of its coal products through a bulk loading terminal which is operated by Westshore Terminals Ltd. Payments for these services amounted to \$20 million for the period April 1, 1985 to December 31, 1985.

In 1985 and 1984 the Company reimbursed a subsidiary of British Columbia Resources Investment Corporation \$2 million and \$1 million respectively for the cost of certain centralized management and administrative services.

16. Segmented Information

	Total		Coal and Port (1)		Oil and Gas (U.K.)	
	1985	1984	1985 (Millions)	1984	1985	1984
Sales						
Export	\$ 602.8	\$ 586.0	\$ 503.0	\$ 494.8	\$ 99.8	\$ 91.2
Domestic	12.1	35.7	12.1	35.7	—	—
	614.9	621.7	515.1	530.5	99.8	91.2
Costs and expenses						
Cost of products sold	433.1	408.7	402.9	383.5	30.2	25.2
General and administrative	11.4	10.9	9.3	9.1	2.1	1.8
Depreciation, depletion and amortization	66.9	73.3	31.0	45.3	35.9	28.0
	511.4	492.9	443.2	437.9	68.2	55.0
Operating profit	\$ 103.5	\$ 128.8	\$ 71.9	\$ 92.6	\$ 31.6	\$ 36.2
Capital expenditures	\$ 69.0	\$ 42.4	\$ 13.3	\$ 12.4	\$ 55.7	\$ 30.0
Property, plant, equipment and related development costs						
Cost	\$ 888.3	\$ 1,052.5	\$ 559.9	\$ 755.9	\$ 328.4	\$ 296.6
Accumulated depreciation, depletion and amortization	254.5	226.0	193.5	191.0	61.0	35.0
Net	\$ 633.8	\$ 826.5	\$ 366.4	\$ 564.9	\$ 267.4	\$ 261.6
Total Assets	\$ 884.6	\$ 1,181.7	\$ 577.6	\$ 662.3	\$ 307.0	\$ 519.4

Note 1: Effective April 1, 1985 the Company sold its investment in its Port Operations (see Note 5).

Note 2: The financial statements include \$285.6 million and \$277.8 million in assets; and \$8.3 million and \$12.0 million in liabilities of the Greenhills Mine Joint Venture in 1985 and 1984 respectively.

Five Year Review

	1985	1984	1983	1982	1981
(Millions except per share data)					
Operations					
Coal shipments — (tonnes)					
— Metallurgical	6.9	7.0	5.7	5.0	6.8
— Thermal	1.2	1.1	.5	.5	.5
Oil production — (barrels)	2.7	2.4	.6	—	—
Revenue					
Coal	\$ 515.1	\$ 530.5	\$ 433.5	\$ 430.6	\$ 511.8
Oil and gas	99.8	91.2	21.2	—	—
Total	\$ 614.9	\$ 621.7	\$ 454.7	\$ 430.6	\$ 511.8
Earnings					
Before extraordinary items	\$ 34.7	\$ 40.9	\$ 60.7	\$ 51.4	\$ 70.5
Net earnings (loss)	(186.8)	26.2	60.7	72.8	70.5
Share Statistics					
Earnings per Common share:					
Before extraordinary items	\$ 1.65	\$ 1.99	\$ 3.26	\$ 2.82	\$ 3.86
Net earnings (loss)	(10.49)	1.18	3.26	3.99	3.86
Dividends					
— Common shares	5.21	—	—	—	9.56
— Preferred shares	2.56	2.56	.62	—	—
Other Financial Data					
Funds from operations	\$ 128.1	\$ 146.0	\$ 137.9	\$ 115.7	\$ 121.3
Capital expenditures	69.0	42.4	180.7	365.8	210.9
Working capital (deficiency)	6.5	5.2	27.1	9.5	(24.1)
Total assets	884.6	1,181.7	1,207.1	1,012.5	663.0
Total long-term debt	549.3	610.4	697.0	639.5	369.4
Shareholders' equity	(12.1)	276.8	247.8	144.7	71.8

Shipments include all coal shipped from the 80 percent owned Greenhills Mine.

Corporate Directory

Directors

- Bruce I. Howe***
Chairman and Chief Executive Officer
British Columbia Resources Investment Corporation Vancouver (a diversified natural resource company)
- Walter J. Riva***
Vice Chairman of the Board
Westar Mining Ltd.
- Jean G. Cormier**
Senior Vice President Corporate Affairs
British Columbia Resources Investment Corporation Vancouver
- Takashi Imai**
Managing Director
Nippon Steel Corporation Tokyo (steel manufacturing)
- Lucille M. Johnstone†**
President and Chief Operating Officer
RivTow Straits Limited Vancouver (a marine, shipyard, aggregates and industrial equipment company)
- Gary K. Livingstone***
President
Westar Mining Ltd.
- Hiroshi Ono**
Senior Managing Director
Nippon Kokan Kabushiki Kaisha Tokyo (steel manufacturing)
- Edwin C. Phillips†**
Retired
Former Chairman and Chief Executive Officer
Westcoast Transmission Company Limited Vancouver (an oil and gas transmission company)
- L. Jack Smith*†**
President and Chief Operating Officer
British Columbia Resources Investment Corporation Vancouver
- Ichiro Sonoda**
Managing Director
Mitsubishi Corporation Tokyo (a trading company)

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Officers

- Bruce I. Howe**
Chairman of the Board and Chairman of the Executive Committee
- Walter J. Riva**
Vice Chairman of the Board
- Gary K. Livingstone**
President
- Robert H. Gronotte**
Senior Vice President, Engineering and Capital Projects
- Thomas A. Beckett**
Vice President, General Counsel and Secretary
- Robert H. Brady**
Vice President, Marketing
- William S. Cameron**
Vice President, Planning and Financial Services
- Robert F. Chase**
Vice President and Chief Financial Officer
- Gary S. Duke**
Vice President, Public Affairs and Government Relations
- Arthur E. Geikie**
Vice President, Human Resources and Administration
- W. Larry Millar**
Vice President, Treasurer
- John A. Powell**
Vice President, Coal Mining Operations
- Robert C. Stanlake**
Vice President, Port Operations
- Michael F. Pang**
Assistant Secretary
- Suzanne K. Wiltshire**
Assistant Secretary

Subsidiary Management

- Robert H. Brady**
President
Westar Mining International Ltd.
- Robert H. Gronotte**
President
Westar Engineering Ltd.
- W. Robert Mendes**
Managing Director
Westar Oil (U.K.)

†Member of Audit Committee

*Member of Executive Committee

Corporate Information

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Minato-Ku, Tokyo 107
Japan
(81-3)402-9547

Auditors

Touche Ross & Co.

Transfer Agent and Registrar

The Royal Trust Company
Vancouver, Calgary, Regina,
Winnipeg, Toronto and Montreal.

Preferred Shares Listed

Vancouver Stock Exchange
The Toronto Stock Exchange

Annual Meeting

The annual meeting of
shareholders will be held on
May 26, 1986.



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